INDEX

721101—46—1

In the Supreme Court of the United States

OCTOBER TERM, 1946

IN THE MATTER OF EQUITABLE OFFICE BUILDING CORPORATION (name changed to "Equitable Office Building Co., Inc."), DEBTOR

No. 609

CHARLES A. DANA, SIR JAMES DUNN, JOHN W. HUBBARD AND NEWCOMBE C. BAKER, AS A COMMON STOCKHOLDERS COMMITTEE, EQUITABLE OFFICE BUILDING CORPORATION, PETITIONERS

v.

J. DONALD DUNCAN, AS TRUSTEE, ET AL.

No. 610

EQUITABLE OFFICE BUILDING 1913 CO., INC., PETITIONER

v.

J. DONALD DUNCAN, AS TRUSTEE, ET AL.

No. 612

ADELAIDE H. KNIGHT AND WILLIAM P. DOYLE, COMMON STOCKHOLDERS OF THE EQUITABLE OFFICE BUILDING CORPORATION, DEBTOR, PETITIONERS

v.

J. DONALD DUNCAN, AS TRUSTEE, ET AL.

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE SECURITIES AND EXCHANGE COMMISSION

The Securities and Exchange Commission became a party to the Chapter X reorganization

proceedings pursuant to Section 208 of the Bankruptcy Act, 11 U. S. C. § 608, and in the courts below supported the petition for a stay of proceedings pending hearings on the merits of the proposed modification of the plan of reorganization.

STATUTORY PROVISIONS

The pertinent sections of the Bankruptcy Act are set out in the Appendix, pp. 15–17.

STATEMENT

Reference is made to the briefs of petitioners for a fuller statement of the facts. For purposes of this memorandum we note only the following salient facts.

The confirmed Plan of reorganization for the debtor under Chapter X of the Bankruptcy Act deals principally with the interests of debenture holders and stockholders. The claims of debenture holders are satisfied in part by common stock of the reorganized debtor and in part by income bonds convertible into stock.[1] The existing stockholders receive one share of new common stock for each 10 shares now held, amounting to 8.4 to 15.4 percent of the new stock issue, depending upon whether or not the new income bonds should be converted. Subsequent to confirmation but prior to consummation of the

[1] The Plan left the first mortgage undisturbed and gave the second mortgage bondholders in the amount of $3,000 their principal in cash, without interest.

plan, stockholders Knight and Doyle (petitioners in No. 612), submitted to the district court a proposal from the City Investing Company to underwrite a modified plan which would afford the common stockholders an opportunity, through purchase of new stock, to pay off junior creditors their full principal and interest and thus retain for the existing stockholders the equity interests accorded to creditors by the confirmed Plan. This proposal was made possible by improved conditions since the date of confirmation. Stockholders not exercising their rights would receive the same stock interest as in the confirmed Plan; in addition, they would enjoy the privilege of selling their rights to subscribe. The underwriters' ability to perform was not questioned and was evidenced by tender of a certified check to the order of the trustee in the sum of $517,258.80, amounting to 10% of the possible maximum commitment.

Without receiving any testimony and without considering the merits (R. 116), the district court denied the petition and refused to stay consummation of the confirmed Plan. The Common Stockholders' Committee (petitioner in No. 609) and the Debtor (petitioners in No. 610) then sought to have the reorganization proceedings dismissed so that the Debtor, utilizing the offer of the City Investing Company, might exercise its equity of redemption in substantially the same manner as was suggested under the Knight Plan.

These petitions, too, were denied. Applications were then made to the Circuit Court of Appeals for the Second Circuit for an order staying the consummation of the Plan pending the outcome of the appeals on the merits; these applications were denied by a divided court.[2] Applications for a stay of proceedings were then filed with Mr. Justice Reed, who, on August 6, 1946, granted a stay pending decision by the full Court upon petitions for writs of certiorari (R. 360–369).

All of the petitioners have filed notices of appeal in the Circuit Court of Appeals for the Second Circuit from the judgments of the district court denying their requests for modification of the Plan or for dismissal of the reorganization proceedings. Only petitioners in No. 612, however, are presently going forward with the appeal in the court below. The Debtor and the Common Stockholders' Committee now seek a writ of certiorari to the Circuit Court of Appeals upon both the refusal to stay the proceedings and for the purpose of determining, prior to the judgment of the Circuit Court of Appeals, whether the action of the district court was proper. Petitioners in No. 612 seek certiorari solely upon the failure of the Circuit Court of Appeals to grant the stay pending appeal.

---

[2] The matter was first heard before Judges Learned Hand, Goddard and Coxe; only Judges Goddard and Coxe joined in the denial order (R. 392).

DISCUSSION

In our opinion the appeals to the Circuit Court of Appeals from the orders of the district court are meritorious and present questions of substantial importance in the administration of the Bankruptcy Act; and a stay is necessary to preserve the *status quo* pending disposition of these appeals on the merits by the Circuit Court of Appeals. This can be accomplished by this Court either by continuing the stay granted by Mr. Justice Reed or by remanding to the Circuit Court of Appeals with directions to enter a stay.

All of the petitioners rest their case on a financing proposal which for the first time would permit salvaging of the bulk of the equity while paying off all matured debts in full. Petitioners in No. 612, two stockholders, sought to alter the confirmed Plan of reorganization by substituting this proposal as a modified plan. The other petitioners asked for dismissal of the Chapter X proceedings following payment of all matured debts pursuant to the proposed financing. In our view compliance with the policy of the Act requires following the plan procedure prescribed by Chapter X, rather than dismissal. However, we agree with all of the petitioners that (1) the district court erred in ruling that the rights of the Debtor and the stockholders were cut off by the order of confirmation, and (2) the existing stay should be continued pending disposition on the merits.

Rapidly changing economic conditions in the post-war period dramatize the need for determination of the rights of security holders of debtors undergoing reorganization to take advantage of such changes. This Court has been confronted with different aspects of that problem in the railroad reorganization cases. See *Ecker* v. *Western Pacific R. R. Corp.*, 318 U. S. 448, 506–509; *R. F. C.* v. *Denver & R. G. W. R. Co.*, Nos. 278–282, October Term, 1945, decided June 10, 1946. We interpret this Court's opinions in those cases as presupposing the right of junior interests to profit by post-confirmation developments which make possible an improvement of their positions without limiting the strict priorities of senior creditors. The denial of a reexamination in those cases rested merely upon a holding that since the valuations under attack had been based upon a long-term forecast as to future earnings, they should not be reexamined merely because of a possibly ephemeral improvement in current earnings. In this case, however, the attempt before the district court to improve upon the confirmed plan and establish the existence of a salvagable equity was not an attempt to reopen an issue of valuation, but was backed by hard money and a responsible underwriting not previously available.

1. Since in our opinion the district court erred, a stay is necessary to avoid hardship to security holders and embarrassment to the reorganization

process. Consummation of the confirmed Plan would entail distribution of new stock to existing debenture holders and stockholders, possible exercise of conversion rights incident to the debentures, and public trading in the securities issued under the plan. Reversal of the orders of the district court and approval of a new plan might then require some of the securities issued under the Plan to be restored to the corporation. The mechanics of tracing the shares of common stock alone would present a monumental problem. In addition, the uncertainties of title would have serious effect upon the public security holders, who could not be sure of their status, and the chaos which reversal of the district court would create would be so great a court might well hesitate before rendering such a judgment. Thus, either the efforts of petitioner to secure relief from an erroneous determination would be prejudiced, or if relief were in fact obtained it would be upon conditions prejudicial to intervening rights.

2. We construe the orders of the district court denying the applications as resting upon a determination that once a plan has been confirmed the reorganization court should not consider a modification—whatever might prove to be its intrinsic merit—which may deprive any class of security holders of advantages conferred by the confirmed Plan. We understand the present posi-

721101—46——2

tion of debenture holders to be that the district court exercised its discretion and found a lack of merit in the proposed plan. However, the record, as we read it, shows the contrary. There was no attempt at weighing the advantages of the modified plan against the old. The district court memorandum opinion in No. 612 reads as follows:

> The deliberate and fully considered adjudication of a responsible court made and entered without objection on the part of any person in interest—and after all parties were afforded ample opportunity to be heard on the merits of the issues involved—and when they and the public—as they had a right to do—confidently relied upon its integrity, should be something more stable than a weather vane on a blustery day in March. For this reason, my consummation order of July 8, 1946, will stand. It follows that the application to reopen the reorganization proceedings of the debtor will be denied. (R. 99.)

When, at a hearing following the filing of the memorandum, an attorney for the bondholders sought to secure a declaration from the bench that the judgment had been rendered on the merits, the district judge replied:

> I simply denied the application. As I said the other day, there manifestly could not be a determination on the merits because I would have to have hearings and

> give notice to all stockholders and all persons in interest, to afford them an opportunity to be heard before I passed on the merits. (R. 116.)

That the district court misconceived the effect of an order of confirmation in barring a new or modified plan is further shown by the court's statement that "It is a question of time" and also by the reference as an analogy to the rule governing redemptions after a judicial sale (R. 138).[3]

We regard as applicable in the context of Chapter X the basic principle of equity which permits a debtor to redeem his property upon full discharge of creditors' claims. This is because the bankruptcy courts are courts of equity without terms, making the entire process of reorganization open to reexamination at any time until the close of proceedings. *Wayne United Gas Co.* v. *Owens-Illinois Glass Co.*, 300 U. S. 131; *Pfister* v. *Northern Illinois Finance Corp.*, 317 U. S. 144, 152.

Section 222 of the Act (11 U. S. C. 622) is a clear statement of the right to modify or alter a plan "after confirmation" and contains a detailed description of the procedure to accomplish any modification sufficiently material to affect adverse-

---

[3] This statement of the rule, as we understand it, appears to be incorrect in failing to recognize that there is a right of redemption after sale, but not after confirmation of sale, which in the present context would be after consummation of the confirmed Plan.

ly the rights of creditors or stockholders.[4] Thus confirmation does not cut off rights.[5] It is merely a step in the reorganization process. ***Wright*** v. *The City National Bank & Trust Company,* 104 F. 2d 285, 287 (C. C. A. 6). Section 226 (11 U. S. C. 626) provides that upon consummation the property shall be "free and clear of all claims and interests of the debtor, creditors, and stockholders." This is inconsistent with an intention to consider the order of confirmation as the act which gives rise to a vested interest in the new securities provided by a plan. Section 236 (11 U. S. C. 636) expressly recognizes that confirmation does not necessarily imply that the confirmed plan will be put into effect as of course. It provides that "if a confirmed plan is not consummated" the court may dismiss the proceedings.

---

[4] Our support of petitioners in No. 612 and our difference with petitioners in cases Nos. 609 and 610 rests on our belief that the statutory safeguards should be adhered to in connection with a consideration of the merits of the new proposals as they affect the interests of stockholders.

[5] We believe it is the consummation of the plan which withdraws "the protecting hand of the bankruptcy court" (*Bell* v. *Roberts*, 112 F. 2d 585, 586 (C. C. A. 3)) and vests in each security holder the new rights. See *In re Ambassador Hotel Corp.*, 124 F. 2d 435 (C. C. A. 2); *Bakers Share Corp.* v. *London Terrace, Inc.*, 130 F. 2d 157, 159 (C. C. A. 2). Prior to that time the property of the debtor is in *custodia legis*, subject to the control of the court so that it may supervise the accomplishment of the "fair and equitable" principles established by the Bankruptcy Act.

The debenture holders rely on Section 224 (11 U. S. C. 624) which speaks of provisions of the plan which are "binding * * * upon all creditors and stockholders," but this section must be read with the provisions of Section 222. Under Section 222 there may be more than one confirmation order if the court finds it necessary to alter the Plan in a material respect after one such order has been entered. Section 224 refers to the last confirmation order entered, for that is the one which will regulate the rights of the security holders.[8] See *In re 1934 Realty Corporation,* 150 F. 2d 477 (C. C. A. 2), certiorari denied, 326 U. S. 734, holding that a district court should entertain a post-confirmation amendment necessary to

---

[8] *Country Life Apartments* v. *Buckley*, 145 F. 2d 935 (C. C. A. 2) and *In re Diversey Bldg. Corp.*, 141 F. 2d 65 (C. C. A. 7), cited by respondents in support of their position, are not inconsistent with our view. In the *Country Life* case the court found that the new plan was neither fair nor feasible nor equitable, and it was apparent that no new factor had arisen after the order of approval which might justify full consideration of a new and different plan. The decision, therefore, apart from the finding of lack of fairness in the new plan, was that the court need not consider it at that particular stage in the proceedings in the absence of any new developments justifying such action. *In re Diversey Bldg. Corp.*, 141 F. 2d 65 (C. C. A. 7) supports our view that it is the consummation of a plan which fixes the rights of security holders, for the debtor in the reorganization proceedings involved in that case sought to amend and modify the plan after the plan had been consummated, eight years after the order of confirmation.

correct inequity revealed by supervening decisions of the New York Court of Appeals and of this Court, although the time to appeal from the order of confirmation had elapsed.

3. The proposed plan shows on its face that in contrast to the confirmed plan it provides for saving of the equity as well as payment in full of the debentures with enough left over for adequate working capital. The offer by the City Investing Company is dramatic evidence of the ability of the enterprise to provide for the retirement of the creditor claims affected by the confirmed Plan.[7] In failing to take testimony and consider the merits of this plan the district court prevented the stockholders from realizing what appeared to be an equity in the debtor's property and allowed that equity to inure to the debenture holders instead.

Although the commitment of City Investing Company, given to the district court on July 16, expired by its terms on October 15, 1946, there is reason to believe that meritorious proposals of the same general character will be available for

---

[7] The Commission regards any discussion of the present value of the debtor's property as irrelevant. Because of the nature of the proposed modification, the pertinent inquiry is whether the district court was warranted in rejecting, without hearing on the merits, an underwriter's proposal which on its face offered the prospect of fully satisfying creditors' claims and preserving for stockholders a larger equity than the confirmed Plan.

consideration on the merits by the district court. Uncertainties inherent in the situation result from the ruling of the district court and the litigation which has followed. Accordingly, we regard this new development as not rendering moot the controversy as to whether the district court has a duty to entertain a meritorious proposal of the same general purport as the one submitted by petitioners.[8]

In urging that this Court limit its review for present purposes to the question of the stay of consummation (in substance the course urged by the petitioners in case No. 612), we do not wish to belittle the importance of the issue which would be presented if the decision of the district court were affirmed on its merits by the Circuit Court of Appeals. However, we do not regard the denial of the stay as necessarily forecasting such a decision by the Circuit Court of Appeals on the merits and, in the event of reversal by the Circuit Court of Appeals, further review by this Court might well be unnecessary. At this juncture we urge only the importance of preserving the status quo pending determination of the appeals to the Circuit Court of Appeals and to this end request that the Court continue the stay either directly or by way of

[8] On November 11, 1946, the Circuit Court of Appeals denied in open court a motion to dismiss the appeals in that court as moot because of the expiration of the commitment.

instructions to the Circuit Court of Appeals to enter an appropriate stay.[9]

Respectfully submitted,

GEORGE T. WASHINGTON,
Acting Solicitor General.

ROGER S. FOSTER,
Solicitor,

ROBERT S. RUBIN,
Associate Solicitor,

GEORGE ZOLOTAR,
Special Counsel,

MYER FELDMAN,
Attorney,
Securities and Exchange Commission.

NOVEMBER 1946.

---

[9] All parties emphasize the importance of the time element, petitioners in Nos. 609 and 610 seeking to shorten the process by urging direct review by this Court. Meanwhile the appeal by petitioners in 612 was argued on November 11, 1946. However, this does not eliminate the necessity of this Court's acting upon the petitions, in view of the suggestion by petitioners in Nos. 609 and 610 that the Circuit Court of Appeals delay decision until this Court has acted upon their petitions for direct review of the district court rulings.

APPENDIX

The pertinent sections of the Bankruptcy Act are as follows:

SEC. 222 (11 U. S. C. 622). A plan may be altered or modified, with the approval of the judge, after its submission for acceptance and before or after its confirmation if, in the opinion of the judge, the alteration or modification does not materially and adversely affect the interests of creditors or stockholders. If the judge finds that the proposed alteration or modification, filed with his approval, does materially and adversely affect the interests of creditors or stockholders, he shall fix a hearing for the consideration, and a subsequent time for the acceptance or rejection, of such alteration or modification. The requirements in regard to notice of hearing, to submission to the Securities and Exchange Commission, to acceptance, to filing and hearing of objections to confirmation and to the confirmation, as prescribed in article VII of this chapter in regard to the plan proposed to be altered or modified, shall be complied with.

* * * * *

SEC. 224 (11 U. S. C. 624). Upon confirmation of a plan—

(1) The plan and its provisions shall be binding upon the debtor, upon every other corporation issuing securities or acquiring property under the plan, and upon all creditors and stockholders, whether or not such creditors and stockholders are affected by the plan or have accepted it

or have filed proofs of their claims or interests and whether or not their claims or interests have been scheduled or allowed or are allowable;

(2) the debtor and every other corporation organized or to be organized for the purpose of carrying out the plan shall comply with the provisions of the plan and with all orders of the court relative thereto and shall take all action necessary to carry out the plan, including, in the case of a public-utility corporation, the procuring of authorization, approval, or consent of each commission having regulatory jurisdiction over the debtor or such other corporation;

(3) if the judge shall so direct, there shall be deposited and distributed, in such manner as the judge may direct, the moneys for all payments which by the provisions of the plan or under this chapter are required to be made in cash; and

(4) distribution shall be made, in accordance with the provisions of the plan, to creditors and stockholders (a) proofs of whose claims or stock have been filed prior to the date fixed by the judge and are allowed, or (b) if not so filed, whose claims or stock have been listed by the trustee or scheduled by the debtor in possession as fixed claims or stock, liquidated in amount and not disputed.

* * * * *

SEC. 226 (11 U. S. C. 626). The property dealt with by the plan, when transferred by the trustee to the debtor or other corporation or corporations provided for by the plan, or when transferred by the debtor in possession to such other corporation or corporations, or when retained by the debtor in possession,

as the case may be, shall be free and clear of all claims and interests of the debtor, creditors, and stockholders, except such claims and interests as may otherwise be provided for in the plan or in the order confirming the plan or in the order directing or authorizing the transfer or retention of such property.

* * * * *

SEC. 236 (11 U. S. C. 636). If no plan is proposed within the time fixed or extended by the judge, or if no plan proposed is approved by the judge and no further time is granted for the proposal of a plan, or if no plan approved by the judge is accepted within the time fixed or extended by the judge, or if confirmation of the plan is refused, or if a confirmed plan is not consummated, the judge shall—

(1) where the petition was filed under section 127 of this Act, enter an order dismissing the proceeding under this chapter and directing that the bankruptcy be proceeded with pursuant to the provisions of this Act; or

(2) where the petition was filed under section 128 of this Act, after hearing upon notice to the debtor, stockholders, creditors, indenture trustees, and such other persons as the judge may designate, enter an order either adjudging the debtor a bankrupt and directing that bankruptcy be proceeded with pursuant to the provisions of this Act, or dismissing the proceeding under this chapter, as in the opinion of the judge may be in the interests of the creditors and stockholders.

U. S. GOVERNMENT PRINTING OFFICE: 1946